

## A Fast-Track Instrument to Update Developing Countries' Tax Treaties

Since the first appearance of the United Nations *Model Double Taxation Convention between Developed and Developing Countries* in 1980,<sup>1</sup> the UN Tax Committee<sup>2</sup> has concerned itself with providing text for tax treaties that better reflects the interests of developing countries. This has been captured in various amendments to the UN Model over recent years.<sup>3</sup> However, developing countries still face a number of difficulties in having those desirable amendments inserted into their existing tax treaties.

The standard approach to amending an existing tax treaty is to negotiate an amending protocol on a bilateral basis. For some developing countries, there are resource constraint issues, with a limited number of officials trained to negotiate amending protocols. For some countries, the treaty partner may be reluctant to schedule a session to negotiate an amending protocol: the treaty partner may already have diary commitments for treaty negotiations, and the developing country is likely to be placed low on the priority list (particularly if there is limited trade and investment with that treaty partner). Requesting an amending protocol may open up a wide range of issues for renegotiation, wider than the developing country would have wished. The treaty partner may be significantly stronger economically, and one-on-one negotiations place the developing country in a position of weakness. There is no current setting which might allow a number of developing countries to negotiate the same amendment at the same time.

Bearing these problems in mind, the UN Tax Committee's Sub-Committee on the Taxation of the Digitalized and Globalized Economy began work two

years ago to consider a streamlined method for assisting developing countries to insert the changes in the UN Model into their existing tax treaties. The result is the *Fast-Track Instrument to Provide for the Streamlined Amendment of Bilateral Double Taxation Treaties* ('the FTI') which was given its second reading at the 28th Plenary Session of the UN Tax Committee in New York on 19 March 2024.<sup>4</sup> The FTI was approved by a majority of the UN Tax Committee and will now go forward with a recommendation from the Committee to the UN Economic and Social Council (ECOSOC).<sup>5</sup>

The draft FTI consists of two parts: a 'framework convention'; and a number of 'schedules'. The framework convention provides a structure and a process through which amendments made to the UN Model can be fast-tracked into specific bilateral tax treaties. The schedules – there are eight attached to the current draft – each contain the text of one recent amendment to the UN Model. The basic idea is very simple: using the setting of the Conference of Parties established under the framework convention, and the process for identifying Covered Tax Agreements and matching the positions of different countries, the specific amendments contained in the schedules can be fast-tracked into existing bilateral tax treaties.

The framework convention is a 'commitment-lite', multilateral convention which establishes the structure and the process. Participation in the framework convention only commits a country to participate in the process: quite explicitly, it does not commit a country to make any particular amendment with respect to any particular bilateral tax treaty that country has

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<sup>1</sup> United Nations, document ST/ESA/102, (New York, 1980) – hereafter 'the UN Model'.

<sup>2</sup> Originally the Ad Hoc Group of Experts on Tax Treaties between Developed and Developing Countries, and, since 2005, the Committee of Experts on International Cooperation in Tax Matters.

<sup>3</sup> Formally, the United Nations Model Double Taxation Conventions between Developed and Developing Countries, current edition 2021 (UN document ST/ESA/378, New York 2021).

<sup>4</sup> The current text of the draft FTI is set out at Annex A of UN document CRP.8, Draft 28th Session Report on the Digitalized Economy, 4 Mar. 2024. The work was referred to in the sub-Committee as 'Workstream A'.

<sup>5</sup> The FTI was approved by a majority, though even the minority generally supported the approach of the FTI. The primary concern of the minority was that they were skeptical as to whether there would be sufficient take-up, particularly from developed countries. To the extent that the opponents of the FTI were from developed countries, and are also government officials, this risks being a self-fulfilling prophesy. Hopefully, however, the countries from whence those individuals come will be prepared to give the FTI a chance. After all, the work of the UN Tax Committee is to develop the UN Model with a view to assisting developing countries. Despite a very open discussion in the Sub-Committee, no clear proposals were accepted that offered an alternative route to ensuring that the amendments to the UN Model find their way into existing bilateral tax treaties with developing countries.

concluded. Thus, the sovereignty and discretion of countries over the contents of their tax treaties is completely preserved. The aspiration, however, is that the existence of the process – to which countries commit by becoming a party to the FTI – will encourage a willingness to make the amendments that have been adopted in the UN Model by the UN Tax Committee.

The framework convention establishes a Conference of Parties that is to meet at least once a year and to provide a setting during which an opportunity will be available for countries to 'speed-date' and agree amendments to their bilateral treaties based on the amendments to the UN Model. This will also allow groups of developing countries to seek to obtain the same amendment in each of their bilateral treaties with the same country. It also provides for a multi-lateral amending protocol to be agreed where the same amendment is to be made to a large number of existing treaties at the same time. The framework convention also provides for the process by which this is to happen.

The standard process is designed to impose as little preparatory work on countries as possible. Each country joining the convention is required simply to review its existing tax treaties and identify those Covered Tax Agreements with respect to which it would be willing to consider making one or more of the amendments set out in the schedules to the FTI (if the other contracting state is also willing to do so). The anticipated output of this listing process is effectively a form of matrix in which each country would list its existing Covered Tax Agreements and indicate which of the schedules it might be willing to apply with respect to each individual treaty, and on what terms (where there is a choice, with regard to tax rate for example). Countries may also, if they wish, indicate the conditions that they would require to agree a particular change: for example, a country might indicate that it would be willing to insert a provision on Automated Digital Services, provided that the other country was willing to agree to include an arbitration provision and an updated Services PE definition. Once these lists of Covered Tax Agreements are deposited, the Secretariat established under the FTI would seek to match potential pairs of willing countries.

In the current draft, countries are not explicitly restricted to the precise wording of the amendments contained in the schedules. However, the entire ethos of the FTI is to limit the amendments to those that have been made to the UN Model by the UN Tax Committee. Hopefully, this should ensure that a request from a

developing country to include some of the UN Model changes will not open up a can of worms and result in the renegotiation of large parts of the existing treaty. More comprehensive renegotiations are, of course, not limited by the FTI. However, it would be inconsistent with the underlying approach of the FTI if this process went beyond making the amendments that have been adopted in the UN Model by the UN Tax Committee.

The schedules to the FTI each contain the substance of one of the recent changes to the UN Model. The format of each schedule contains a draft Amending Protocol which makes the amendment to the specific bilateral tax treaty to give effect to the change to the UN Model. Each draft Amending Protocol has blanks to fill in which are necessary to complete the Amending Protocol.<sup>6</sup> In some cases, the schedule contains alternative wording to reflect the majority and minority views expressed in the UN Model.<sup>7</sup>

The 'output' of the FTI process is, therefore, a series of Amending Protocols, each of which makes the UN Model amendments to the specific treaty.<sup>8</sup> Taking as its 'output' the traditional concept of an amending protocol, the FTI uses this well-established technique to amend existing treaties, rather than trying to reinvent the wheel. The use of an established tool to amend treaties means that existing constitutional provisions and parliamentary procedures for approving amending protocols should be applicable.

The draft FTI which was approved by the UN Tax Committee contains eight schedules, reflecting a number of recent changes to the UN Model. These changes are: the inclusion of specific reference to pension funds; a provision on offshore indirect disposals; a provision on Fees for Technical Services (reflecting Article 12A of the UN Model); a provision on Automated Digital Services (reflecting Article 12B of the Model); a UN-style provision on arbitration; a UN version of the Subject To Tax Rule; a provision on capital gains arising from immovable property; and an updated provision on the definition of a Services PE. A key feature of the FTI is that it is open-ended and new schedules can be added to the FTI by the Conference of Parties when those amendments to the Model are adopted by the UN Tax Committee. Only the Tax Committee can amend the UN Model, but the Conference of Parties can then add a new schedule accurately encapsulating the amendment to the Model. The FTI is specifically designed to be flexible and take on board future changes to the UN Model.

Assume, for example, an existing bilateral tax treaty with a developing country which is in need of updating. A

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<sup>6</sup> For example, it is necessary to fill in the details of the tax treaty that is being amended, it is necessary to identify the article(s) being amended, some provisions require a rate of withholding tax to be agreed, all require dates when the changes come into effect, and there may be a choice of language option.

<sup>7</sup> In the form of Arts 2A and 2B etc.

<sup>8</sup> Where a pair of countries agree to make several amendments to the same treaty, the amendments set out in the different schedules can be combined into a single Amending Protocol so that only one document needs to be concluded between the two contracting states.

single amending protocol might be agreed that, for example, includes provisions on pension funds, offshore indirect disposals, a provision on fees for technical services, an arbitration provision, and a subject to tax rule, all in the same Amending Protocol. Aside from supplying the details required by the draft Amending Protocols, no further drafting would be required by the negotiating team from the two countries.

One area where the FTI may particularly come into its own is with regard to the introduction of the new UN Subject to Tax Rule in a large number of treaties already in existence with developing countries.<sup>9</sup> A single session of the Conference of Parties might lead to a multilateral amending protocol inserting this Subject to Tax Rule into a large number of treaties.<sup>10</sup>

While the standard process requires limited work on the part of countries signing up to the FTI, there is also an enhanced procedure for those countries that want a higher degree of automation in the amendment of their tax treaties (but who are willing to do rather more work in advance to achieve this automation). In that case, the countries concerned would need to elect for the enhanced procedure and supply with their list of Covered Tax Agreements all of the information necessary to fill out a completed Amending Protocol (rates of tax, numbers of the articles to be amended, dates of amendments, language version etc.). Assuming that two countries both elect for this enhanced procedure, and that the Secretariat matches the positions of those two countries, the Secretariat would produce a draft Amending Protocol using the details provided. That Amending Protocol would then become binding on the two countries unless within a month they decided to back away from the agreement. This enhanced procedure requires more upfront work by countries (as opposed to the standard procedure which requires very little upfront work) but does achieve a degree of automation of treaty amendment.

The FTI will, no doubt, be compared with the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ('the BEPS MLI'). There are some similarities, in that both seek to streamline the amendment or modification of existing treaties, but there are significant differences. The BEPS MLI imposes a binding legal obligation on parties to the convention with respect to their Covered Tax Agreements to make the specific amendments or modifications unless they adopt one of the reservations to the particular articles (which is why

many countries that have signed the BEPS MLI have entered reservations, except with regard to the mandatory minimum standards). By contrast, the FTI imposes no binding legal obligation to make any specific amendment to any particular treaty. The only obligation is to be willing to participate in the process. The BEPS MLI itself is a legally binding instrument which amends or modifies treaties (except where reservations apply) and so constitutional requirements and parliamentary procedures have had to be applied to the BEPS MLI, which has proved difficult or impossible in the case of some countries.<sup>11</sup> By contrast, the output from the FTI is the standard, and well-recognized, form of an amending protocol, which should present no such difficulties. While the BEPS MLI could, in principle, be used for future amendments to the OECD Model, it was not explicitly designed for that purpose. By contrast, the FTI is designed to be flexible and enduring and to encompass future amendments to the UN Model. Perhaps most significant, because of its legally binding nature, the BEPS MLI imposed significant burdens on the relevant experts in each contracting state before signing the BEPS MLI and depositing the interim and final positions of states. By contrast, the FTI is designed to impose very little prior obligations on the competent persons in tax authorities. While the BEPS MLI has led to a proliferation of synthesized texts, the FTI – using the format of amending protocols – should not lead to a necessity to create synthesized texts.

Given the current discussions at the United Nations towards a Framework Convention on inclusive and effective cooperation on tax matters,<sup>12</sup> some analogies may be drawn with the FTI. However, the FTI is a completely separate project, that began prior to the General Assembly Resolutions which paved the way for the Framework Convention on cooperation. It so happens that the FTI also adopts the structure of a framework convention and a Conference of the Parties, but this is very different from the framework that is being contemplated in respect of the UN institutional and substantive dialogue. There is absolutely no reason why the FTI should be tied up in any way with the discussion of a UN Framework Convention, nor should it be regarded as a suitable subject for a protocol to the proposed Framework Convention.

What happens next with the FTI is a transmission by the UN Tax Commission to ECOSOC with a recommendation that the draft FTI be taken forward as a multilateral convention. Given the support of a majority of the

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<sup>9</sup> The text of the Subject to Tax Rule can be found at the Co-Coordination Report: Proposal for the inclusion of a general 'subject to tax' rule in the United Nations Model Double Taxation Convention between Developed and Developing Countries, document E/C.18/2024/CRP.8 (Mar. 2024).

<sup>10</sup> It might be noted that amendments to tax treaties are not restricted to sessions of the Conference of the Parties. There is no reason why the FTI process cannot be used to agree amending protocols by online and remote processes.

<sup>11</sup> Germany and Sweden, e.g., are countries that have been unable to simply bring the BEPS MLI itself into effect in their legal systems. Amending protocols have been needed instead.

<sup>12</sup> See the material at UN Tax Convention | Financing for Sustainable Development Office.

members of the UN Tax Committee (and no technical objections from any member of the Committee to the approach adopted), there is every reason to be optimistic that ECOSOC will adopt the recommendation of the Tax Committee. At that point, the UN Office of Legal Affairs is likely to become involved in taking the draft FTI and recommending any changes necessary to open the document up for signature as a multilateral convention. Given that the participation in the FTI is explicitly designed not to restrict national sovereignty or discretion over tax treaties, and that the FTI reflects changes to the UN Model that have already been adopted, it is hoped that a large number of countries will agree to participate in this process.

Will the FTI be successful in streamlining the amendment of developing countries' tax treaties? At this point in time, no one can answer that question. The FTI is an entirely novel type of instrument, designed with input from the UN Tax Committee, with a view to streamlining the amendment of tax treaties. In principle, it should work. If the FTI is successful, it may offer a new pattern for the streamlined amendment of large numbers of tax treaties to reflect, in the future, both changes to the UN Model and perhaps even changes to the OECD Model.

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